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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FOUR

ASIAN SQUARE, INC.,

Plaintiff and Appellant,

v.

JAMES WONG, et al.

Defendants and Respondents.

A152308

(San Mateo County
Super. Ct. No. CIV529052)

The sham pleading doctrine allows a court to disregard allegations in an amended complaint that are inconsistent with those in an original complaint, where the new allegations are intended to avoid attacks raised in a demurrer and there is no satisfactory explanation for the inconsistency. (*Deveny v. Entropin, Inc.* (2006) 139 Cal.App.4th 408, 425–426 (*Deveny*).) Based primarily on this doctrine, the trial court sustained demurrers to all of plaintiff’s claims and dismissed this action. We conclude the sham pleading doctrine is inapplicable in the circumstances before us, and accordingly reverse the judgment.

I. BACKGROUND

The procedural history of this case is complex, involving an original complaint and five amended complaints, but the underlying facts are not. In brief, plaintiff alleges that, before his death, Alan Wong was the president of plaintiff, Asian Square, Inc. In January 2009, he borrowed \$5 million in the name of plaintiff without authorization, pledging plaintiff’s property as collateral, and used the proceeds of the loan for his own

personal benefit. Defendants are the personal representatives of Wong’s estate and the successor trustees of a trust Wong created.

Plaintiff brought this action on June 12, 2014, more than five years after Wong took out the loan. In an effort to avoid the bar of the statute of limitations based on a theory of delayed discovery, plaintiff amended its original complaint to allege it did not learn of the loan until “a substantial period” afterward. This effort was defeated after defendants demurred based in part on the argument that plaintiff must have learned of the unauthorized loan well before mid-2010. In amended pleadings, plaintiff then alleged it had learned of the loan in 2009 and that Wong and plaintiff had agreed that Wong would repay the loan from his own resources.

Relying primarily on the sham pleading doctrine, the trial court ultimately sustained demurrers without leave to amend and dismissed the case. Nothing in the pleadings, papers, or judicially noticed facts suggests that the later allegation—that plaintiff learned of the loan in 2009—is inaccurate.

We will discuss the allegations of the various complaints and the trial court’s ruling in more detail below as necessary to understand the issues plaintiff raises on appeal.

II. DISCUSSION

A. Standard of Review

In reviewing a judgment dismissing an action after the trial court sustained a demurrer without leave to amend, we assume the truth of all facts pleaded in the complaints, as well as those which may reasonably be inferred from them, and we also consider facts of which the trial court properly took judicial notice. (*Cantu v. Resolution Trust Corp.* (1992) 4 Cal.App.4th 857, 878 (*Cantu*); *Professional Tax Appeal v. Kennedy-Wilson Holdings, Inc.* (2018) 29 Cal.App.5th 230, 233–234 (*Professional Tax Appeal*).) Our review is de novo. (*Professional Tax Appeal*, at p. 233.)

B. The Sham Pleading Doctrine Does Not Bar the Amendments

1. The Early Pleadings and Third Amended Complaint

The original unverified complaint alleged Wong acted without plaintiff's knowledge or consent when he used the proceeds of the loan for his personal benefit. It asserted causes of action for conversion, breach of fiduciary duty, money had and received, and fraudulent transfer.¹ Defendants demurred, contending all causes of action were barred by the applicable statutes of limitations, which ranged from two years to four years. (Code Civ. Proc., §§ 337, 338, subd. (c), 339, 343; Civ. Code, § 3439.09, subd. (a).)

Plaintiff then filed a first amended complaint, which added allegations that Wong fraudulently concealed from plaintiff that he had obtained the loan and that plaintiff did not discover these facts "until a substantial period of time after said acts took place." Defendants again demurred, asserting all causes of action were time-barred. In its opposition to the demurrer, plaintiff argued its claims were not time-barred because Wong fraudulently concealed his actions, leading to delayed discovery. In response, defendants argued the fraudulent concealment theory was not pled with particularity and that "[i]t is frankly not possible that Plaintiff did not know about a \$5 million lien on its property for a year and a half." They sought and received judicial notice of the minutes of a March 11, 2009 board meeting, at which plaintiff's board of directors removed Wong as president.

The trial court sustained the demurrer without leave to amend as to the cause of action for breach of fiduciary duty and with leave to amend as to the remaining causes of action. Inter alia, the court ruled plaintiff must allege specific facts showing delayed discovery of Wong's actions.

¹ The complaint also included causes of action for "additional money had and received" and open book account, both alleging Wong borrowed money from plaintiff and owed a balance of \$899,020.67. This alleged loan amount is not pertinent to the issues on appeal.

Before the hearing on the demurrer to the first amended complaint, plaintiff's attorney had made a request to be relieved as counsel. Represented by new counsel, plaintiff filed a second amended complaint, then, with leave of court, a third amended complaint.

The second and third amended complaints alleged that Wong took out the unauthorized loan on or about January 29, 2009, and that plaintiff discovered this conduct later that year. Specifically, the third amended complaint alleges that "[s]ome months later and also in 2009," the remaining directors and shareholders learned of the loan, the terms of which required payments over a period of five years, ending in February 2014, and learned Wong had taken the proceeds for his personal benefit. From that time forward Wong and Asian Square "understood by their conduct and behavior" that Wong or his trust would be responsible for repaying the loan without using the income or assets of Asian Square. This "implied-in-fact agreement" avoided a legal dispute between Wong and plaintiff's majority shareholder, who was a family member. Beginning in 2009, Asian Square relied on Wong's conduct in making payment on the loan. Wong and/or his trust made the required payments on the loan until his death in 2013, and others acting on behalf of Wong, his trust, or his estate continued to make the payments until January 2014. The third amended complaint asserted causes of action for breach of implied-in-fact contract, unjust enrichment, money had and received, open book account, and fraudulent transfer (Civ. Code, §§ 3439.04, subd. (a)(2)(A) & 3439.05).

Defendants demurred to the third amended complaint and moved to strike portions of it. The trial court sustained the demurrer without leave to amend as to the causes of action for breach of implied contract and unjust enrichment, concluding they violated the sham pleading doctrine because there was an irreconcilable conflict between the first amended complaint, which implicitly alleged that that plaintiff did not know of the fraudulently concealed loan until at least May 2010, and the allegation of the third amended complaint that plaintiff learned of the loan and formed an agreement regarding repayment of the loan in 2009. The court treated the motion to strike these causes of action and supporting allegations as moot. It sustained the demurrer to the cause of

action for fraudulent transfer with leave to amend, and overruled the demurrer to the other causes of action. The court also granted defendant's motion to strike the allegation that defendants unjustly retained the benefit of the loan proceeds, on the ground there was no separate cause of action for unjust enrichment.

2. *Sham Pleading*

Plaintiff's primary contention on appeal is that the trial court erred in applying the sham pleading doctrine. "Under the sham pleading doctrine, '[i]f a party files an amended complaint and attempts to avoid the defects of the original complaint by either omitting facts which made the previous complaint defective or by adding facts inconsistent with those of previous pleadings, the court may take judicial notice of prior pleadings and may disregard any inconsistent allegations.' [Citation.] Where no explanation for an inconsistency is offered, the trial court is entitled to conclude that the pleading party's cause of action is a sham and sustain the demurrer without leave to amend." (*Zakk v. Diesel* (2019) 33 Cal.App.5th 431, 447; accord, *Deveny, supra*, 139 Cal.App.4th at pp. 425–426; *Amarel v. Connell* (1988) 202 Cal.App.3d 137, 144 (*Amarel*) [sham pleading rule applied where allegations in prior complaint that are " 'destructive of the cause of action . . . are omitted in the subsequent pleading without a valid explanation' "].) The doctrine is "not intended to prevent honest complainants from correcting erroneous allegations or to prevent the correction of ambiguous facts." (*Hahn v. Mirda* (2007) 147 Cal.App.4th 740, 751.) It should be applied in conformity with its purpose, " 'which is to prevent an amended pleading which is only a sham, when it is apparent that no cause of action can be stated truthfully.' " (*Amarel*, at p. 144.)

Earlier pleadings may not be considered "to bind the pleader to an untrue and erroneous admission against interest which was inadvertently contained therein, but which has been subsequently disavowed and corrected in an amended pleading filed by leave of court, in which, or accompanying which, satisfactory explanation is made of the reason which caused the original erroneous statement. . . . If courts were to bind litigants to inadvertent untrue statements of facts and forbid them the inherent right to correct the false by substituting the true facts, they would become partisans to miscarriages of

justice.” (*Jackson v. Pacific Gas & Electric Co.* (1949) 95 Cal.App.2d 204, 211.) Similarly, the court in *Macomber v. State* (1967) 250 Cal.App.2d 391, 399 (*Macomber*) explained that the sham pleading doctrine properly may be used to “discourage sham and untruthful pleadings,” but concluded the doctrine was not properly applied to the case before it, which was “not a situation where the contradiction of the original allegation carries with it the *onus of untruthfulness*.” (Italics added.)

The recent case of *JPMorgan Chase Bank, N.A. v. Ward* (2019) 33 Cal.App.5th 678 (*JPMorgan Chase*) is instructive. The plaintiff there, Chase, sought to foreclose a loan secured by real property. The verified complaint alleged that the borrower erroneously executed the deed of trust in his individual capacity, although title was vested in the borrower in his capacity as trustee of the borrower’s trust. (*Id.* at p. 681.) After the borrower’s death, the successor trustee demurred, asserting that the complaint’s allegations confirmed that the trust never executed a written instrument conveying the property and that any action for relief from fraud or mistake would be time-barred. (*Id.* at p. 682.) Represented by new counsel, Chase opposed the demurrers, claiming the gravamen of its action was to enforce the deed of trust as written, not to correct a mistake in its execution. The trial court sustained the demurrers without leave to amend, and the appellate court reversed. (*Id.* at pp. 682–683.) As relevant here, it concluded that denial of leave to amend was an abuse of discretion, notwithstanding the sham pleading doctrine. It noted that the sham pleading doctrine was not meant to be “ ‘mechanically applied,’ ” and that “ ‘the rule must be taken together with its purpose, which is to prevent [an] amended pleading which is only a sham, when it is apparent that no cause of action can be stated truthfully.’ ” (*Id.* at p. 690.) The court noted that the complaint was drafted by prior counsel and Chase immediately distanced itself from the allegation in responding to the demurrer. The court presumed that new counsel and further legal research “revealed the fallacy of the assumption that [the borrower’s] signature had to specify that he signed as trustee in the name of the Trust,” and concluded the original allegation was not “the assertion of a foundational fact that should bind Chase in all subsequent proceedings.” (*Id.* at 692.)

The situation before us is unusual. The first amended complaint alleged plaintiff did not learn of the loan for “a substantial period of time.” The length of that time is not specified, but plaintiff—with some quibbles not relevant to our analysis—does not quarrel with the trial court’s conclusion that the allegation implies that plaintiff acquired its knowledge no earlier than some time in 2010, so as to bring this action within the longest applicable limitations period, four years. In support of their demurrer to the first amended complaint, defendants pointed out that plaintiff terminated Wong’s employment in March 2009, shortly after the loan was taken out, and argued that it was “frankly not possible that Plaintiff did not know about a \$5 million lien on its property for a year and a half.” But defendants are trying to have it both ways—having demurred on the ground plaintiff must have known about the loan well before 2010, they now take the position that plaintiff is barred by its previous pleadings from *agreeing* with them on this factual issue. Defendants have drawn our attention to no cases holding a plaintiff may not amend a complaint in similar circumstances. (See *Macomber, supra*, 250 Cal.App.2d at p. 399 [sham pleading doctrine inapplicable where new, contradictory, allegation does not carry “onus of untruthfulness”]; *Larson v. UHS of Rancho Springs, Inc.* (2014) 230 Cal.App.4th 336, 344 (*Larson*) [court will disregard “ ‘falsely pleaded facts’ ”]; *Cantu, supra*, 4 Cal.App.4th at p. 878 [having admitted his knowledge of fact, plaintiff “cannot now inconsistently *and falsely* allege to the contrary”], italics added.)

The cases applying the sham pleading rule consistently note that a plaintiff may not amend a complaint to omit harmful allegations without a satisfactory explanation. (*Deveny, supra*, 139 Cal.App.4th at pp. 425–426; *Larson, supra*, 230 Cal.App.4th at p. 344; *State of California ex rel. Metz v. CCC Information Services, Inc.* (2007) 149 Cal.App.4th 402, 412; *Vallejo Development Co. v. Beck Development Co.* (1994) 24 Cal.App.4th 929, 946.) A “ ‘plausible’ ” explanation may be “the need to correct a mistaken allegation or to clarify ambiguous facts.” (*Smyth v. Berman* (2019) 31 Cal.App.5th 183, 195; accord, *Contreras v. Blue Cross of California* (1988) 199 Cal.App.3d 945, 950.)

The record here sheds no direct light on how the first amended complaint came to include the misleading allegation. But it does show that the complaint was not verified, and that shortly after filing it plaintiff's original counsel sought to be relieved as counsel based on "irreconcilable differences" with plaintiff. When new counsel began working on the case, he promptly filed an amended complaint alleging that plaintiff learned of the loan in 2009 and that from that time on all parties understood that Wong would be responsible for repaying the loan with his own assets. In opposition to the demurrer to the third amended complaint, plaintiff's new counsel submitted a declaration stating that after he was retained to represent plaintiff, he reviewed the pleadings and documents and conducted an investigation of the facts relating to the timeliness of the claims. This investigation "confirmed that it was a period of months before the [unauthorized] loan was discovered by the Plaintiff, but that nonetheless, i[t] was discovered in 2009." While "[s]ome months later" is not squarely inconsistent with the ambiguous phrase "a substantial period of time," at the hearing on the demurrer new counsel forthrightly told the court that his predecessor had been "frankly ill advised" in trying to plead around the statute of limitations with this vague allegation. He went on to explain that as soon as he began working on the case, he recognized the problem with the statute of limitations, investigated the matter, and learned that in 2009, members of plaintiff's board learned about the loan and fired Wong, and that they learned Wong was tending to the problem and making the loan payments. Plaintiff's new counsel explained that he therefore amended the complaint to allege the date of discovery truthfully.

This explanation passes the bar of being a reasonable explanation, particularly in light of the fact that the third amended complaint alleged a date of discovery consistent with the position taken by defendant. The purpose of the sham pleading doctrine is to " 'prevent [an] amended pleading which is only a sham, when it is apparent that no cause of action can be stated truthfully.' " (*JPMorgan Chase, supra*, 33 Cal.App.5th at p. 690.) The new alleged date of discovery is not suspect, and the sham pleading doctrine does not require us to disregard it. The trial court thus erred in sustaining the demurrer to the third amended complaint's causes of action for breach of implied contract and unjust

enrichment on this ground. For the same reason, the trial court should have denied plaintiff's motion to strike portions of the third amended complaint to the extent the motion was based on the sham pleading doctrine.

3. Fourth and Fifth Amended Complaints

Plaintiff amended its complaint twice more. As relevant to this appeal, the fourth amended complaint realleged the first and second causes of action—breach of implied-in-fact contract and unjust enrichment—“for appellate integrity only,” and included factual assertions regarding plaintiff learning of the unauthorized loan and its understanding with Wong that he would repay the loan. Based on the sham pleading doctrine and the previously sustained demurrers, the trial court struck these portions of the fourth amended complaint.

Plaintiff then filed a fifth amended complaint, which omitted the stricken allegations and asserted only two causes of action: one for money had and received, and one for open book account. The court sustained the demurrer to the money had and received claim without leave to amend, concluding that without the previously stricken allegations, there were insufficient allegations to support a theory of equitable estoppel, and the cause of action was hence barred by the statute of limitations. Upon the parties' stipulation, the court also sustained without leave to amend the cause of action for open book account.

The pertinent portions of the rulings regarding the fourth and fifth amended complaints were based on the trial court's previous conclusion, in connection with the demurrer to the third amended complaint, that the sham pleading doctrine barred plaintiff from pleading it learned of the unauthorized loan and formed an agreement with Wong regarding repayment in 2009. Because we conclude the trial court erred in reaching this conclusion, its subsequent rulings striking the allegations and sustaining the demurrer to the cause of action for money had and received necessarily fall as well.

C. Unjust Enrichment

As an independent basis to sustain the demurrer to the third amended complaint's cause of action for unjust enrichment (the second cause of action), the court concluded

there is no separate cause of action for unjust enrichment in California, and granted defendants’ motion to strike paragraph 23 of the third amended complaint, which alleged defendant received the benefit of the unauthorized loan proceeds and unjustly retained them. The court relied on *Levine v. Blue Shield of California* (2010) 189 Cal.App.4th 1117, 1138, which states, “ ‘ “[T]here is no cause of action in California for unjust enrichment.” ’ ” (Accord, *Durell v. Sharp Healthcare* (2010) 183 Cal.App.4th 1350, 1370.)

There is some conflict in the case law as to whether California recognizes an independent cause of action for unjust enrichment. One approach was taken in *Rutherford Holdings, LLC v. Plaza Del Rey* (2014) 223 Cal.App.4th 221, 231, which explained, “ ‘ Unjust enrichment is not a cause of action, however, or even a remedy, but rather “ ‘ “a general principle, underlying various legal doctrines and remedies” ’ [Citation.] It is synonymous with restitution.” ’ ” The court construed the cause of action labeled “unjust enrichment” as a quasi-contract claim seeking restitution. (*Ibid.*) But the court in *Professional Tax Appeal, supra*, 29 Cal.App.5th at p. 238, recently treated a claim for unjust enrichment as a stand-alone cause of action, explaining “[t]he elements of a cause of action for unjust enrichment are simply stated as ‘receipt of a benefit and unjust retention of the benefit at the expense of another.’ ” (Accord, *Prakashpalan v. Engstrom, Lipscomb & Lack* (2014) 223 Cal.App.4th 1105, 1132.) Whether the claim is treated as one for unjust enrichment or as a mislabeled claim in quasi-contract, we conclude the label does not preclude a court from considering the substance of the cause of action.

Defendants argue that plaintiff is barred from seeking equitable relief on a quasi-contract theory because it is also asserting a legal claim for breach of contract. For this proposition, they cite *Klein v. Chevron U.S.A., Inc.* (2012) 202 Cal.App.4th 1342, 1387–1388, which is one of a number of cases holding that a plaintiff may not pursue a quasi-contract claim if the parties have an enforceable contract regarding the same subject matter. These cases, however, appear to concern *express* contracts, rather than contracts implied in fact. (*Klein*, at p. 1384 [contract for sale of gasoline based on Chevron’s

advertised price per gallon]; *Newport Harbor Ventures, LLC v. Morris Cerullo World Evangelism* (2016) 6 Cal.App.5th 1207, 1222, review granted March 22, 2017, S239777, affirmed (2018) 4 Cal.5th 637 (*Newport Harbor*) [“Quantum meruit recovery is inconsistent with recovery for breach of written contract”]; *Grebrow v. Mercury Ins. Co.* (2015) 241 Cal.App.4th 564, 580; *California Medical Assn. v. Aetna U.S. Healthcare of California* (2001) 94 Cal.App.4th 151, 172 [“[A] quasi-contract for unjust enrichment does not lie where, as here, express binding agreements exist and define the parties’ rights”]; *Lance Camper Manufacturing Corp. v. Republic Indemnity Co.* (1996) 44 Cal.App.4th 194, 203 [“[A]n action based on an implied-in-fact or quasi-contract cannot lie where there exists between the parties a valid express contract covering the same subject matter”]; *Wal-Noon Corp. v. Hill* (1975) 45 Cal.App.3d 605, 613 [“There cannot be a valid, express contract and an implied contract, each embracing the same subject matter, existing at the same time”].)

The court in *Newport Harbor* explained that a party may plead inconsistent counts “ ‘[w]hen a pleader is in doubt about what actually occurred or what can be established by the evidence.’ ” (*Newport Harbor, supra*, 6 Cal.App.5th at p. 1222.) Application of this rule is appropriate where, as here, any contract was not express, but rather allegedly formed by the “conduct and behavior” of the parties. Construing the second cause of action as one for quasi-contract, we conclude the trial court erred in sustaining the demurrer to it and striking paragraph 23 of the third amended complaint.

Defendants argue that, even if plaintiff may plead an equitable claim for quasi-contract, the claim is untimely. But they did not demur to this cause of action in the third amended complaint on this ground, instead relying solely on the sham pleading doctrine, and we will not consider the issue now. We express no view on the timeliness of the second cause of action in the third amended complaint, and nothing we say is intended to preclude defendants from raising the issue in any appropriate manner on remand.

III. DISPOSITION

The judgment is reversed. The matter is remanded for further proceedings consistent with this opinion. Plaintiff shall recover its costs on appeal.

TUCHER, J.

WE CONCUR:

STREETER, Acting P. J.

BROWN, J.